Philip Morris and RJR, has turned its strategic focus to profitability, rather than share. Additionally, Liggett gained +0.5 pts. of discount share in 1994, which could help lend support to industry stability.

Exhibit 3

Share Trends	% Premium Share 1993	1994	1995E	% Discount Share 1993	1994	1995E	Total Share 1993	1994	1995E
Philip Morris	49.7%	53.6%	54.9%	29.4%	26.5%	25.4%	42.2%	44.8%	5.3%
RJR Nabisco	27.1%	23.5%	22.7%	36.6%	33.1%	32.3%	30.6%	26.7%	5.8%
Lorillard	10.7%	10.6%	10.8%	0.8%	1.0%	0.9%	7.1%	7.5%	7.6%
"Oligopolists"	87.5%	87.7%	88.4%	66.7%	60.7%	58.6%	79.9%	79.0%	8.7%
B & W	6.3%	6.7%	10.8%	19.0%	20.9%	33.9%*	11.0%	11.3%	8.3%
American	5.1%	4.7%	---	9.5%	13.1%	---	6.7%	7.4%	---
Liggett	1.1%	0.9%	0.8%	4.8%	5.3%	7.6%	2.4%	2.3%	3.0%
"Disrupters"	12.5%	12.3%	11.6%	33.3%	39.3%	41.4%	20.1%	21.0%	21.3%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%
Memo: Seg %	63.2%	67.5%	67.5%	36.8%	32.5%	32.5%	100.0%	100.0%	100.0%

* Includes 1.7% of discount share from brands from American Tobacco B&W will eventually sell, per FTC agreement

5. Profit growth soared in 1994. Industry profits soared +20% in 1994, compared to 1993's (45)% decline during the price war. Volumes grew 6%, due in part to inventory liquidation in 1993, and perhaps also to a slight up-tick in consumption patterns. Net revenue growth per unit for the full year was (4)%, but +7-8% in second-half 1994 versus second-half 1993. Industry margins improved by approximately 5-6 pts, contributing about 18 points to industry profit growth, as all major players slashed headcount and promotional spending during 1994 to match the lower prices implemented mid-1993.

Exhibit 4: 1994 Domestic Tobacco Industry Statistics

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	Unit Vol(B)	%Chg v YA	Op. Pr ($M)	%Chg v YA	Profit /Unit	%Chg v YA	% Margin	%Chg v YA
Philip Morris USA	219.3	+13	$3,302	+18	$15.06	+4%	38.9	+3.3
RJR USA	130.3	-7	1,475	+23	11.32	+33	34.0	+8.0
B & W (Est.)	55.4	+10	600	+50	10.83	+37	33.5	+10.3
Lorillard	36.6	+12	610	+3	16.67	(8)	41.1	+2.4
American	36.3	+17	248	+32	6.82	+13	21.2	+4.7
Liggett (Est.)	11.5	+2	10	+488	0.87	+400	3.0	+2.4
Total	489.7	+6	$6,245	+20	$12.75	+13	35.0	+5.5

Even though we believe a price increase in likely built into stock prices, investors may be becoming somewhat jittery about when the industry will actually take a list price increase, especially since the last list price increase was in November, 1993 (all players cut off-invoice allowances on discount brands last Spring). We originally expected a increase prices in November or December of 1994, since the industry had raised prices every year since 1980 in November or December. Uncertainty surrounding the Federal Trade Commission's (FTC) hearing related to Brown & Williamson's purchase of American Tobacco likely delayed this. We anticipate an industry-wide $.04-$.05/pack

price increase, likely led by RJR, during the next few weeks; this translates to increases of +4-5% on premium brands, 7-8% on discounts, and 5-6% overall. We believe that RJR has little excess marketing accrual cushion available to use as a boost to 1995 profits to achieve our estimated +4-5% operating profit growth in 1995 -- unless it takes pricing. Conversely, we estimate Philip Morris has built up approximately $450 million in potential over-accrued expenses, worth some $0.30/share. Even without an increase in pricing, we feel PM USA can achieve our 10% profit growth forecast in 1995. If we don't see price hike in 1995 -- which we would place a low probability -- we could potentially reduce our RJR earnings estimates by ($0.09)/share.

6. Risks: Will Joe Camel attempt to knock the smile off the Marlboro Man? If Marlboro continues to gain share at the same rate as 1994 (Marlboro gained +4.5 share pts. during 1994), we could see RJR take more aggressive steps to combat share loss. Importantly, however, we don't believe RJR would take such extreme steps to regain market share as to force a hostile competitive reaction from Philip Morris, or other competitors. Additionally, given that Philip Morris' management expects Marlboro's share to return to historical growth trends (+0.5 pts. per year), perhaps management would be willing to give up some share gains above this trend, if it lent to industry stability. We strongly doubt either company wishes to experience another price war.

GARY BLACK 212-756-4197
JON ROONEY 212-756-4504

END OF NOTE

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